

STATE BOARD OF LAND COMMISSIONERS

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Pete T. Cenarrusa, Secretary of State
Alan G. Lance, Attorney General
J. D. Williams, State Controller
Anne C. Fox, Superintendent of Public Instruction

Stanley F. Hamilton, Secretary to the Board

FINAL MINUTES GRAZING AND CROPLAND SUBLEASING SUBCOMMITTEE MEETING April 1, 1998

A meeting of the State Board of Land Commissioners Subcommittee for grazing and cropland subleasing was held April 1, 1998 at 9:00 a.m. in the fourth floor training room of the Joe R. Williams Building.

Subcommittee members present were:

Attorney General Alan G. Lance
State Controller J. D. Williams

Stanley F. Hamilton, Director, Idaho Department of Lands, Secretary to the Board

Ben Ysursa, Secretary of State's office sat in for Secretary of State Pete Cenarrusa.

Others present at the meeting were:

Clive J. Strong, Office of the Attorney General
Jay Biladeau, Asst. Director Lands, Minerals, Range, Idaho Dept. of Lands
Tracy Behrens, Range Management Specialist, Idaho Dept. of Lands
Bryce Taylor, Chief, Bureau of Range Management & Surface Leasing, ID Dept. of Lands
Jean Smith, state grazing lessee

The meeting was called to order by Attorney General Lance. The concept of grazing subleases was discussed. An acceptable form needs to be developed for the sublessee to sign whereby he/she would promise to fulfill all the terms, conditions and provisions of the lease. Staff needs to make a determination as to whether or not the sublessee is a qualified bidder pursuant to Idaho Code.

If it is determined they are a qualified bidder, the Land Board does not have to get involved in the subleases. If it is determined they are deemed to not be a qualified bidder, then the Land

Board will have to make the decision.

Also to be discussed will be the fee charged for an application for a sublease.

Director Hamilton passed out the minutes of the first subcommittee meeting and a briefing memorandum on the issue. Director Hamilton stated that Tracy Behrens has researched information from other states who do subleasing. He asked Tracy to walk through the current policy and what other states are doing. Then the group can discuss what recommendation to make to the full Land Board.

Mr. Behrens referenced the board memorandum for the current policy on subleasing. The current policy is identified under IDAPA rules. The department subleasing policy is further explained in the department's Operations Memorandum (OM) 1521.5 on Subleasing. This OM will be updated when direction is received from the full Land Board.

The current policy requires advanced authorization to enter into a sublease agreement. The lessee must submit a written request that includes the name and address of the sub-lessee, a copy of the proposed sublease agreement, and a \$50.00 application fee. In conjunction with the recently implemented Vegetation Management Policy, the department also requires the sub-lessee to submit a management proposal indicating how the state land will be managed.

The department does not require prior authorization for a lessee to take in herd stock or to pasture another rancher's livestock as long as the state lessee maintains control of the management of the lease. There is also no limit in the number of times a sublease can be authorized during the ten-year lease.

Mr. Behrens then covered the policies currently used in Montana, Arizona, Wyoming, Utah, and Oregon. The information collected from the other state land management agencies indicates that the majority of them either currently assesses a sublease fee, or are considering a proposal to collect a fee. Three different methods are used to collect the sublease fee. The methods are: a percent of the payment to the rancher above the standard state rental fee, a flat rate per AUM above the standard state rental fee, and a percent surcharge above the standard state rental fee.

Mr. Behrens said that the department recommends that the Land Board modify the existing sublease policy to include a sublease surcharge in the range of 25-50% of the current state AUM rate. The remaining current policies of advanced notification, \$50 processing fee, and management proposal should remain in effect.

Mr. Taylor stated that this meeting is intended to deal with grazing subleases. Any other subleases should be addressed differently because of the differences. Director Hamilton said especially cottage site leases that are significantly different.

Attorney General Lance stated that he was having a difficult time ascertaining why it is that we should charge significantly more for subleasing. The AUM is a variable and that is how the lease rate is established – as he understands it. He stated he was having some philosophical

problems as to why we would go back and add on to that because it is a sublease.

Mr. Behrens stated that the situation that is faced is that when a state lease is subleased, generally they receive a payment in excess of what the state grazing fee is. The department has documentation where the lessee is receiving up to three times the state AUM fee for subleasing his allotment.

Controller Williams said he felt the problem is that all AUM's are not created equal. He stated that there is some very good pasture that the state is not getting market value out of it. An enterprising operator can sublease and make a lot of money. He said he does not feel this happens a lot, but he likes the idea of partnering up with the lessee. If there is more money to be made, the state should share.

Clive Strong, Division Chief, Natural Resources Division said he wondered why the state should not get all the difference because the central premise – when you do a grazing lease – is that the persons bidding for – and part of the qualification criteria is that it is an integral part of their operation. If during the term of the lease, they can turn around and lease out that property, then the question really becomes – is it integral to their overall operation. Aren't you setting up a situation, by allowing subleasing, you are encouraging people to speculate. He stated that there is a fiduciary duty to think about in terms of why – if this is no longer integral to the operation, why shouldn't it be going out to the open market and reestablishing market value.

Attorney General Lance asked how many subleases there were in a year. Director Hamilton thought somewhere between 6-12 at the most. This does not include herd stock leases. That is a different issue.

Mr. Taylor said there were 3 subleases last year and there are currently 4 pending. Herd stock arrangements - if someone is short on livestock then they take stock in from someone else and run them with their own. They then maintain full responsibility of full lease control. These are more common.

Mr. Strong asked how the subleases were factored into the range management plan. Mr. Taylor said that the management plan did not change. They are still obligated to the same AUM's that are allocated to the property and the same rotation applies. Mr. Strong asked why the sublessee should not be bound by the same management proposal that the lessee has. Attorney General Lance said that the sublease signature or form that is developed needs to clearly specify that this is the case. Director Hamilton said that while the department wants to know what the management proposal is and it is locked in under the lease, management proposals ought to be able to change. All of the details ought not to be locked in stone over the 10-year lease. The lessee might have a little better idea about how they want to operate and the department needs to be able to deal with that. Mr. Strong said that he didn't mean that they should be bound in but he should not be relieved of that obligation.

Mr. Taylor said under current policy, the sublease agreement is subject to department approval.

Mr. Behrens said that in all the sublease agreements currently held, the subleases do incorporate land ownership other than the state lands. They are for the ranchers base property,

federal lands or other ownership, but the subleases are not just tied to the state land.

Mr. Taylor stated that the management plan with the lessee is the real contract. He said he did not believe the department would relieve him of any of that responsibility just because he is subleasing his rights to someone else. He would still be held responsible to the department.

Mr. Strong asked what the process would be with the property going from the lessee, to the sublessee and back to the lessee. How would the changes be handled. Mr. Behrens stated that in most cases, the land base stays the same, it is just the operator that changes.

Attorney General Lance asked Mr. Strong to have a failure to report a sublease as grounds for cancellation.

Mr. Taylor said the department would like guidance from the board whether to limit the number of subleases allowed each lessee during a 10-year lease period. He said from his perspective and from talking to the industry, he did not feel that subleasing should be encouraged but should be allowed.

Controller Williams said we have only a few total subleases, however, we have a lot of pasturing arrangements. He said that is where the money is. Mr. Strong said it seemed to him that you establish criteria – there has to be some demonstrated management reason why it is being done. There should be a business justification for it. If you set a high fee or perhaps take the entire excess amount then you discourage this type of arrangement unless there is a true, legitimate business reason for doing it. Is it simply profiteering?

Controller Williams said if we're partnering with these people and they are pasturing, who cares – we'll make more money. Mr. Taylor asked Controller Williams if he was suggesting that instead of just addressing subleasing, should it be expanded to include pasturing. Controller Williams stated absolutely, there is no money in subleasing, the money is in the pasturing side. The school children need a cut of this.

Director Hamilton said there are two ways this is happening. One is that the arrangement is – let me take over your state ground and I will operate under your lease. The other is, I will turn the cattle over to you – maybe for a surcharge for herding and management. One is called herd stock and the other is not so well defined.

Mr. Taylor presented a case from McCall on herd stock.

Attorney General Lance said it appeared to him that unless we address that issue, if we put too many limitations on the concept of subleasing or the price of subleasing is too high, it's easily subverted by doing this arrangement. We need to bring both of them up together.

Controller Williams suggested coming up with a percentage. If you're going to sublease or pasture on state ground, you are going to have to give the state x number of dollars which is a percent of what they are getting. The lessee will have to disclose what he is getting per AUM.

Mr. Taylor stated there is no handle on how many are pasturing. In the past the department has

had the right to require lessees to take in herd stock if they are below their stocking number. That has been a part of our standard process. If a lessee only has 50 head of stock and the land will support 100, the lessee only wants to pay for 50. The department has said no – find 50 more and pay for the 100 that there is feed for. This could create some problems.

Controller Williams stated there are a lot of AUM's we're not getting market value from. Someone is making off with the money.

Attorney General Lance asked why individual parcels weren't evaluated for AUM potential. Controller Williams said it used to be done that way but was changed several years back.

Mr. Strong told Attorney General Lance that to go out and evaluate each parcel on its own basis wouldn't work. Mr. Strong asked if the lessee could be requested to disclose as part of his application whether or not he intended to do any pasturing. If they do, set the terms and conditions up front on what percent of that pasturing the state would get.

Mr. Taylor said there is another issue at hand in the pasturing agreement. If you're pasturing livestock, if you are doing the fencing, salting, riding and the doctoring then the operator, in the industry, will get something for his labor. Mr. Strong said that would be taken into consideration and could be done up front.

Mr. Taylor said that sometimes this doesn't occur up front. Ben Ysursa said they still have to report it. Mr. Strong said they have to disclose it if it occurs during the lease.

Attorney General Lance asked Mr. Ysursa if the Secretary of State would be interested in evaluating AUM's on each parcel. Mr. Ysursa – speaking on behalf of the Secretary of State – said he is not interested in examining each piece of property and coming up with different AUM's. AUM's lag behind 1 ½ - 2 years.

Mr. Ysursa said the carrying capacity is a key point.

Mr. Jay Biladeau said there is another issue that determines value and that is market demand. We inventory the parcels so we have a pretty good handle on carrying capacity. In the 70's the department got out and gathered market data throughout the state for those types of uses – spring, summer etc. He thought the rate varied from about 3-6 dollars an AUM at that time. They since have gone to a state rate. This was done by a strong push from industry. Director Hamilton stated that was probably one of the harder fought discussions that the Board has been involved in.

Controller Williams said Mr. Strong has mentioned trying to get the money up front in the bidding costs. At least have it disclosed up front. Mr. Strong stated that it should be put in the lease – if you have pasturing agreements, these pasturing agreements must be reported. Controller Williams stated there are two major categories of pasturing – one is a turn-key operation where the animals are dropped off at the gate and picked up in the fall. The operator does everything. This should be factored into the provisions. The other is where they come out and take care of the animals themselves. He suggested if it is a turn-key deal, we take 25% of the increase rate. If it is not a turn-key deal, we take 50%. Throw this idea out to the industry and find out what

their reaction is.

Attorney General Lance said he did not think we would ever be able to plug the hole. There are ways to get around it. He said we need to maintain sufficient flexibility. He said he felt the Board needs to give the staff guidelines – formulas.

Mr. Strong suggested the board could add the following into the lease. If you enter into a pasturing agreement, you must report this to the Board. There must be approval and the Board will take a percentage. Then the Board could set up a policy guidance memo that would say – In these types of situations, this is what we normally do, but give the discretion to the board to charge a greater/lesser amount based on the facts.

Director Hamilton said that a considerable amount of this needs to be done at the staff level. The staff needs direction and when we run out of direction, then staff needs to come to the Land Board.

Attorney General Lance said that staff and legal counsel need to develop a definition of subleasing, which not only incorporates the traditional sense, but also pasturing, herd stock, etc. in one definition.

Controller Williams said then we need to look at it again, then have industry look at it. Attorney General Lance said, in talking with staff, they don't want to let the initial lessee off the hook. There would not be a release of responsibility.

Director Hamilton said that the department would have to look at the rule and consider an amendment of it. The lease term needs to be looked at. There are a couple of different terms that might have to be incorporated. The Department has an Operations Memorandum that basically takes Board policy and explains to staff how it is to be implemented. We are not quite ready to amend that but can begin to work on it. We will need a good sublease form, specifically for the formal sublease, and also for herd stock, pasturing agreements as well. Eventually we will talk about a fee. The fee should be set at policy rather than rule.

Attorney General Lance asked if there should be a limitation on how many times a lessee can sublease. Mr. Strong said he would like the discretion to look at defining the two different situations and putting some fairly severe restrictions on subleases. Subleases are really a mechanism to avoid the bidding process whereas a pasturing agreement is something that is facilitated.

Attorney General Lance said this has to do with a percentage of the rate of gain. We are kind of getting into a quagmire relative to computation of really what the lease formulas are. Attorneys General Lance said when everyone is ready, call another meeting to go over in terms of what will be recommended to the Land Board.

Mr. Taylor said that there were four (4) current requests for sublease approval before the department at this time. They need to be dealt with. He asked if the department should bring these before the Board at the May meeting. Mr. Behrens said that all four that are pending are from last year. They are one-year requests. Attorney General Lance said that an agreement

has been made with them and he said he did not feel that we could plug in the new rules on these.

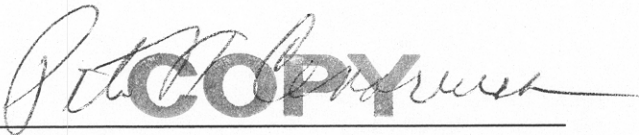
Attorney General Lance said staff needs to determine what staff time would be to process a sublease application and that ought to be the application fee. Director Hamilton said that could be done.

There being no further business, the meeting adjourned.

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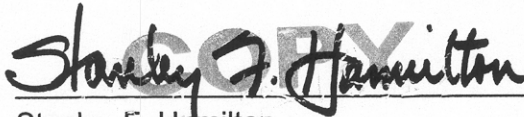
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President, State Board of Land Commissioners and
Governor of the State of Idaho

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Pete T. Cenarrusa
Secretary of State



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Stanley F. Hamilton
Director, Idaho Department of Lands